

**LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS**

200 W. Washington, Suite 301
Indianapolis, IN 46204
(317) 233-0696
<http://www.in.gov/legislative>

FISCAL IMPACT STATEMENT

LS 7144

BILL NUMBER: HB 1358

NOTE PREPARED: Jan 14, 2004

BILL AMENDED:

SUBJECT: Tax Deduction for Overseas Military Service.

FIRST AUTHOR: Rep. Van Haaften

FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: X GENERAL
X DEDICATED
FEDERAL

IMPACT: State & Local

Summary of Legislation: The bill provides that an Indiana resident who is serving outside the United States on active duty in the armed forces is entitled to an income tax deduction for the first \$12,000 of income received during the taxable year for the individual's military service.

Effective Date: January 1, 2005.

Explanation of State Expenditures: The Department of State Revenue (DOR) would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate this deduction. These expenses presumably could be absorbed given the DOR's existing budget and resources

Explanation of State Revenues: The bill would reduce state Adjusted Gross Income (AGI) Tax liabilities of individual taxpayers who serve in the military outside the U.S. or its territories, and whose income earned from military service exceeds \$2,000. The revenue loss due to this bill could potentially total about \$900,000 in FY 2006. This assumes the number of military personnel with Indiana residence serving overseas in future years is comparable to the total reported by the U.S. Department of Defense for 2003. It also assumes that all such personnel are able to claim the full \$12,000 exemption.

Background: The bill provides for a deduction from AGI of up to \$12,000 for income earned for military service outside the U.S. or its territories during the taxable year. This deduction could be claimed by a qualifying taxpayer in lieu of the existing \$2,000 maximum allowable deduction for military service pay.

According to the Defense Manpower Data Center, 2,499 enlisted personnel and 147 officers (including warrant officers) reporting Indiana as their state of residence to the Internal Revenue Service served outside

the U.S. and its territories during the first 9 months of 2003. The average taxable income during this period for the enlisted personnel was \$13,457 and for the officers was \$27,693. Based on these averages, it is assumed that each individual would be able to claim the maximum allowable deduction of \$12,000 under the bill. The total deduction amount would be about \$31.8 M. However, each individual is entitled to a \$2,000 deduction for military service pay under current statute - estimated to total about \$5.3 M. Thus, the net additional deductions that could potentially be claimed by these individuals under the bill is estimated to total about \$26.5 M, with a tax impact totaling about \$900,000 annually.

The revenue from the AGI Tax on individuals is deposited in the state General Fund (86%) and the Property Tax Replacement Fund (14%). Since the deduction is effective beginning in tax year 2005, the fiscal impact would begin in FY 2006.

Explanation of Local Expenditures:

Explanation of Local Revenues: Because the proposed deduction would serve to decrease taxable income, counties imposing local option income taxes (CAGIT, COIT, and/or CEDIT) may, as a result, experience an indeterminable decrease in revenue from these taxes.

State Agencies Affected: Department of State Revenue.

Local Agencies Affected: Counties with a local option income tax.

Information Sources: Deborah Williamson, Defense Manpower Data Center, 831-583-2400.

Fiscal Analyst: Jim Landers, 317-232-9869.